Sense 67
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Corporate Image and Those Magic Multiples. Special Interviews with: Gus Levy of Goldman Sachs Gordon Williams of Business Week Tom Johnson of Chemical Bank

When asked about corporate image, a well-known financial expert gave what is perhaps a classic definition: "Look at U.S. Financial, it grows 25% per annum and has a P/E multiple of 10. IBM, on the other hand, grows about 15% a year yet its multiple is 40. That difference in multiples *is what I call corporate image.*"

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Let's Talk About Wall Street by Walter P. Margulies

Every corporate plan, goal and hope of company management hinges on one essential ingredient: That the investor places a sufficient value on the securities of the company to support management's programs. In brief, without Wall Street backing, the best-laid plans of mice and men will come to nought.

In an economic world of growing complexity, in a decade when 26 million Americans own shares in U.S. corporations (more than double a brief dozen years ago), and in a day when criteria for effective business policy are shifting as rapidly as they are today, it is not surprising that the financial community is also searching for new variables in determining the intrinsic present and future value of every company.

For the American business community—as managers and investors both—the implications of this reevaluation are gigantic.

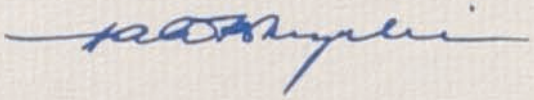
Yesteryear's product marketing strategy may no longer suit the changing taste and values of today's consumer. The old ways of maintaining and increasing the value of a company's securities have also passed into history. The composition, taste, style, financial instruments and criteria of the investing public today are as different from those of the late Sixties as today's headlines are different from those of yesterday.

In indicating the changes in the financial marketplace of the Seventies, we have sought to bring to bear on the evaluation of corporate communications with Wall Street not only the sophisticated thinking of financial practitioners and policy-makers, but also the theory that dominates the horizon of the thought-leaders in major universities. At times, practice leads theory. In other periods, theory is clearly ahead of practice.

In developing effective corporate communications approaches for major companies in the U.S. and abroad, we take into account the best thinking and greatest scope of experience from all valid sources—practitioners and theorists alike.

Therefore, in presenting some of the provocative new views about the relationship of corporate management with the investor, in this issue, we are basing our comments, perceptions and ideas on a combination of practical experience and academic theory. The academic literature about security valuation is proliferating rapidly. In this issue of *Sense*, we have synthesized and incorporated some of the trends that are only now emerging.

We would like to encourage you, our readers, to contribute to this essential discussion and debate by sharing your thoughts and experience with us. For those who might like to delve further into academic financial theory, we will provide an up-to-date bibliography of current literature upon written request.



"Stocks Aren't Bought; They're Sold."

"Stocks aren't bought; they're sold," says one top-notch, long-experienced broker, and therein lies the secret of corporate communications strategy.

Once we assume that a security is a "product" that is bought by and sold to a customer community like any other product (at the highest level of abstraction, and without analyzing the specific marketing and promotion strategy at this point), then we have opened up a pandora's box. If it is a reasonable assumption that promotion and corporate "visibility" play a large role in the movement and acceptance of other "products" (be they consumer products, consumer services or industrial products), then we should take promotion directly into account when determining or forecasting the value of a firm and the price of its securities.

There is a good deal more than mere intuition to guide us in making this statement and in using this approach.

We have overfilled archives of empirical evidence showing that corporate communications influence Wall Street. Innumerable examples show the measurable impact of "good news" and "bad news" or favorable and unfavorable information on the price of a stock. For instance, when a top man leaves the helm of a highly visible company to head up another or to go into government, it isn't unusual for the stock of his original company to dip, if only temporarily. Obviously, Wall Street considers management a critical factor in the success or failure of any firm, and this evaluation is reflected immediately in the price the firm's securities command.

The management, product and marketing strategy of a company are microscopically studied by the specialists on Wall Street. There isn't any sophisticated investor today who relies solely on past performance and financial ratios as an indicator of any company's future profitability.

Furthermore, it's logical that the activities of the highly visible firm have a larger impact on the stock price and multiple than those of a lesser known rival. The direction of this impact is clearly a factor of the corporate news or information content and its historic reliability. Not only does the professional investor form an over-all judgment about a company and its securities from its continuing communications program, but he also evaluates individual news items about the firm's activities in terms of their anticipated effect on corporate profitability in the short- and long-run.

In security valuation theory, on the horizon of the newest developments of financial theory, there is a considerable amount of literature to back up the contention that the marketability of an issue is an important factor in determining the price or intrinsic value of that security. So far, however, marketability has been defined more in financial terms than in terms of marketing experience.

For instance, in 1967, Professor John Shelton studied the relationship between the price of a warrant and the price of its associated stock. He took marketability into account by differentiating between securities listed on the Amex and those not listed. The very fact that "visibility" in the form of such listing was taken into account by a financial theoretician and academician indicates that the discipline is moving in the direction we're considering here.

Other leading theoreticians, such as Professor Myron Gordon in his study of the valuation of a corporation, used the size of the issue as a proxy for marketability. Again, we find the academician confined, perhaps too narrowly, to the variables familiar to his discipline. In the graduate schools, business administration, finance and marketing continue to occupy different floors and often even different buildings, not only physically, but intellectually.

Nonetheless, there is growing realization among financial theorists that it's the facts behind the figures that count. The experimental work in universities today is concentrated in the development of financial models for security valuation and forecasting that take communications, marketing and other behavioral variables directly into account.

In this issue of *Sense*, we will develop one aspect of this theory of the valuation of a firm, showing the influence of corporate communications and information programs. With our discussion, we will also present the comments of three leading spokesmen of the financial community, who, themselves or through their work and their firms, play a significant role in the presentation, trading, and valuation of major companies' securities.

There are relatively few single product-line companies of significance left in the U.S. today. The move has been to diversification and conglomerization to achieve greater efficiencies and profits. Yet, as these amalagamations have solved some problems, they have at the same time created others of a totally different nature; one of the most important being—corporate communications.

The relevant question in shaping a communications strategy, therefore, might well be phrased: How can management of a modern company pull together the wide variety of corporate activities and profit centers into an effective program communicating its strengths to the investment community?

In order to answer this question, we have brought together in this issue not only our practical experience coupled with up-to-date academic theory, but also the views and experience of the financial community which is the target for such communications efforts. We chose, by design, three totally disparate leaders of the financial community, each with his own sphere of influence and his own particular perspective.

Gus Levy's reputation as the crusty, outspoken managing partner of venerable Goldman Sachs & Company has long been legendary. A tough-minded, no-nonsense financier of prodigious experience, he is not one to mince words for the sake of maintaining Wall Street's cherished low profile among professionals. His judgment, backed up by one of the Street's most diverse and knowledgeable research staffs, has been the compelling cause for major mergers, acquisitions, divestitures, new issues, huge syndicated flotations. If there were a Hall of Fame among investment bankers, Gus Levy would be assured of his niche in it.

Gordon Williams' influence and perspective are both quite different from the direct impact of a Gus Levy. As former financial editor and now associate editor of *Business Week*, he is a continuing, direct and highly skeptical target of business and financial news, be it through press conferences, management interviews, or the sheer tonnage of releases that overflow his in-box at every mail delivery. As a journalist, he brings to the analysis of financial news both the knowledge of security analysts who are part of his readership and the innate doubting-Thomas attitude that is essential to his craft. The management that can convey a point to him, past a professional cynicism groomed through years of experience, will have scored an important point indeed.

A new school of financial decision-makers is represented by Chemical Bank's Tom Johnson. As corporate planning vice president of one of our leading commercial banks, Tom Johnson is in a pivotal position between the corporate community and the financial world. In the spirit of management styles of the Seventies, he views the financial community less as a solo virtuoso like some of the financial whizzes of earlier eras, but more as a member of a management team who orchestrates the diverse functions into a cohesive whole.

Obviously, no three men can stand for a complex investment community that spans some 26 million individual and institutional investors. However, as a sampling and taste of the diversity of interests that combine to influence and lead Wall Street, these three spokesmen do reflect a number of the prevailing attitudes and thoughts.

Each of our three guests speaks in the idiom of his own craft and skill, not as professional communicators, but rather as men who are continuously judging the communications of others, in order to sift the wheat from the chaff. The questions they raise and the opinions they voice underscore the changed tenor of the times.

In the Sixties, the jargon of Wall Street was replete with fancy ratios and mechanistic formulae that have long since passed through computers into oblivion. In the Seventies, it is human judgment, supported by painstaking research, that has reemerged as the critical factor in the practitioners' pragmatic approach to security valuation. And this judgment, as articulated by our three guests, is very consciously influenced by the marketing and communications skills of the managements trying to convey their companies' strengths to the financial market-makers.

As Gordon Williams points out, "We are in an era when conglomerization has outrun communication. Companies may have learned how to create new types of corporate structures, but they still have a lot to learn about corporate communication . . ."

However, the need is often father to the system. And as business historian Bruce Chandler pointed out some years ago, "structure follows strategy." Today, when diversification and conglomerization seem like a viable answer to certain seasonal and cyclical problems inherent in being a one-product company, it is unlikely that corporate strategists will turn back the clock. Conglomerization is probably here to stay for a long time to come. The communications strategies required to sustain this new form of business are as different from the communications strategies of yesteryear as the corporate structure is different from the proprietorship.

Here are the views and words of three leading financial men. In one way or another, they are indicative of the thousands of professionals in Wall Street whose good opinion of a company and its future will determine tomorrow's prices for that company's securities.

Question: *What criteria do you consider most important in determining the value of a company and its future?*

Levy: Bricks and mortar are nothing; it's people. It all depends on management. The quality of the product and its acceptance are also important in the evaluation of a company's worth. So, it comes down to product and management. People who recommend investments want to know everything about a company, but especially about management. Credibility is essential. Corporate and financial officers charged with communicating with Wall Street analysts must be on the level—and must not kid them.

As for service-based companies versus manufacturing, services are well regarded. They have no inventory and their accounting is simple. Also, services are growing faster than the GNP. Services are a growth industry and they command pretty good multiples. For example, earnings of hospitals and nursing home companies tend to be stable, not volatile, contrary to general impression.

In communicating with Wall Street, corporate management should be available to analysts and newsmen, and tell everything they can, the good and the bad. We find out the bad anyhow, and then we don't believe them again. SEC Chairman Casey has come out in favor of public forecasts by companies. I like that.

Question: *How far into the future do you discount earnings?*

Levy: Three to five years is the pattern.

Question: *Does it vary by industry?*

Levy: Consumer goods are more easy to forecast than steel or machine tools. You figure consumer goods with the growth of GNP and forecast.

Question: *How do you value R&D?*

Levy: It's very important, as a percentage of sales. Those who spend more, generally do better. In the case of one consumer company I'm associated with, 30% of the products they sell now didn't exist two to three years ago. The company that spends more does better. Drug companies spend more than any industry and their multiples are among the highest.

Question: *Do you differentiate between basic research and commercial R&D?*

Levy: It's difficult to separate product development from basic research. It's a combination of both. There is also much use of in-house marketing research now—it's been the pattern over the last few years. You prize that highly. It's a good idea. It doesn't mean they don't use outside research too, but it means better control.

The criteria I consider important in looking at a situation—after all, we're buying the future—is how responsive the management and company are to the customer community. Are they good corporate citizens—in community activities and philanthropies?

Question: *What does that tell you about them?*

Levy: That they're interested and informed, and concerned with the well-being of their employees and community.

Question: *Does it also preclude future problems?*

Levy: That kind of activity may preclude future problems.

The main thing, in my opinion, is the importance of maintaining the credibility of management and the integrity of the product.

Question: *What makes for that confidence?*

Levy: The first thing probably is the industry the company is in. In some industries a good growth rate is very believable; in others, it's harder to visualize.

The second thing that is extremely important is what the company has done over a long period of time. If it has had a 15% growth rate over 10 years, then the burden of proof is heavy on him who says that it won't continue.

For example, since World War II, Avon has been well thought of by investors. It has had 25 years of 20% growth, and for the past 15 years, people have been saying that it can't go on. Avon has sold at 50 times earnings! Their strength is their method of merchandising, including going abroad with it, and in finding some good opportunities for new investments over the years.

On the other hand, if a company has grown at 2% and suddenly it predicts 20%, then the burden of proof is on them. The long-term record is important. It is an input into the P/E. For example, it's easier to understand drug and cosmetics growth than steel.

Another important factor in confidence is the way management relates with the financial community. How believable they are. How accurately they forecast in the past. Take Masco. We worked with Masco over 10 years ago. They produce single-handled faucets. The company had no investment standing. But they've grown pretty steadily at 20% a year. What do they have?

An able management, good growth of product, very well conceived and profitable acquisitions, good relationships with the financial community, and a high degree of management confidence.

P/E ratios are a state of mind, not a science. Few will argue that. The market may be weak, but institutional investors come in because they have confidence in a specific company.

Gordon L. Williams, Associate Editor, *Business Week*

Question: *What kind of news about a company does the financial community want?*

Williams: Obviously it wants to learn everything about a company it can—who it is, what it does, where it has been, where it is going. Most of all, I guess, it wants to know where the company is going—how much it is going to grow.

What we provide at *Business Week* is an interpretation of events, with special reference to their effect on business. Like the financial community, we are interested in everything that affects the investment decision.

We want to know about current and anticipated earnings; the product areas the company is in and how well they are doing; where the company is going over the longer haul—the next two or three years, through the next economic cycle, over the next decade. We want to know where a company is weak. And, of course, we want to know about the skeletons in the closet.

The best thing that any company can do is provide all the information it can, because it is going to be found out anyway, by the financial press and by the securities analysts, not to mention the competition and the regulators. Bad news comes out whether you want it to or not and it is better if management tells the story itself, even if it hurts, than to have it break through another source. A *mea culpa* by corporate management is better in the long run than a damning denunciation by someone else.

Question: *How do professionals on Wall Street use information to develop earnings forecasts?*

Williams: It tends to be a mathematical formula approach, based on industry information and information the company has made available, and what is written about a company in the financial press.

But I am not necessarily writing to inform the professional stock market analyst. Our audience is the sophisticated business executive, though he may not be a specialist in the areas I am writing about. My specialty is finance, but I have to write it so it can be read not only by the financial officer but by the marketing man and the production man and the staff lawyer. Our audience is total corporate management.

Question: *How much emphasis do you place on writing about management as against writing about a product?*

Williams: We write about both. We put Polaroid on the cover recently and, of course the story told a lot about Dr. Land as a manager, but it also told a lot about how the company is expanding its manufacturing facilities so it can produce its own camera. When we tell a story, we try to tell a pretty complete story. And we try to put it into some sort of context. We try to avoid the isolated story. It is a constantly moving economy and business climate and we look for stories that illustrate the times.

Question: *How can a company help provide you this kind of news?*

Williams: Most companies have become fairly sophisticated about communicating with the press. Of course, we are buried under a deluge of earnings reports, speeches, management changes. A lot of it is purely smoke, and some of it is pretty bad.

Many companies still find it difficult to talk about themselves and prefer to operate out of the spotlight. Most businessmen still aren't awfully comfortable about talking with the press. I can sympathize with that at times. They are afraid of exposing themselves to the

eyes of the regulatory agencies and the competition. But they often use poor judgment about what outsiders already know and they often under-estimate the good they might be able to do themselves by telling their story.

Question: *Does a strong corporate image help communicate a company's story?*

Williams: Sure. It is only natural. I will first automatically turn to material from the companies I regard as industry leaders, simply because I do think of them as the leaders, the guys who are doing the important, exciting things. There are some companies where you simply know that what they are doing will generally be innovative and exciting.

And the other side of the coin is equally true. We are all turned off by a company that tries to make up in sheer volume for a lack of meaningful communication.

I am very annoyed by companies that can't bother to update mailing lists, or send us 15 or 20 copies of the same stuff. We have companies that send material to people who have not been here for years, to people who are now dead. We had one company that regularly sent material to an editor who has been dead for years and they still sent it to *The Business Week*, even though we dropped *The* from our title in the 1930s. We tend to have doubts about that kind of a company.

Obviously, the company that communicates well is way ahead of the company that does not. Maybe it shouldn't be that way, but it is. You pay more attention to the companies that impress you and the company that gets the right material to you at the right time is going to do better in the financial press and on Wall Street than the company that cannot be bothered.

Question: *Will an effective image help a company in trouble?*

Williams: Well, nothing will really help a company that is in trouble, but if a company that people regard as basically honest and square gets into trouble, it will tend to get a more favorable hearing. You tend to think of the trouble as a passing thing, as something that couldn't be helped.

Question: *What's your view of corporate advertising in business publications?*

Williams: Well, a look at who I work for ought to answer that one for you, but really it goes beyond that. I really read our advertising and I find it helps me keep up with what is happening in the world of business. And that is important to me.

In an era of mergers, acquisitions, diversification, it is easy to lose sight of who is who and what is what. Take all of the changes in corporate names, for instance. The company itself has changed drastically from what it used to be. It makes new products, sometimes not even the products it started out making. And then the name changes and instead of an old, familiar name, you have initials or an acronym. It is too easy to forget a company's antecedents and what it is today and who owns it and what it owns. And then the company has lost touch with the public, including the investing public.

We put out a quarterly survey of corporate earnings each quarter and each time we get new names and old ones disappear and you say, "Who's that?" It always was RCA to most people, so it was okay to drop the cumbersome Radio Corp. of America. But who remembers that something called A-T-O used to be Automatic Sprinkler? I have to think twice to remember that Bancal Tri-State is what used to be Bank of California. When

Continental Illinois Bank of Chicago became a holding company it became Conill Corp. and not many people remembered that, so they had to go back to the Continental Illinois name.

Some of it gets pretty far out. LTV gave up control of its old LTV Electrosystems business, so the LTV label had to come off. That was fine. But they made it E-Systems and who can remember that?

A company may have a good reason for changing its name, but when it does it is going to have to take some time and trouble to explain it—what, where and why. Or else people are going to forget them and that obviously isn't good.

Question: *What do you regard as being effective marketing-oriented communications today?*

Williams: I am not really sure you can separate out marketing and financial communications today. The public is sophisticated, alert. When ITT got into trouble last spring, it was over a merger—a financial deal. But when the story got into the press, an awful lot of people found out for the first time that ITT makes bread and runs hotels. Some people stopped using Saran Wrap when Dow Chemical was making napalm.

A lot of things have changed in the age of conglomeratization and diversification and companies have a lot to learn about communicating in this age. Companies are trying to reach so many different audiences today —the portfolio manager and the financial writer and the housewife—and it is hard to keep the messages separate. I am not sure you can, but obviously companies have to try. It doesn't make much sense for Gulf & Western to spend a lot of money trying to tell the movie-goer that they own the Hollywood company that made "Love Story" and "The Godfather." But Gulf & Western has to get that message across to the investor because then he will buy Gulf & Western stock.

We are simply in an era when conglomeratization has outrun communication. Companies may have learned how to create new types of corporate structures, but they still have a lot to learn about corporate communication—who to reach with what message, how to reach them, and so on.

At *Business Week*, we are in the business of finding company stories and writing them and that is what Wall Street is doing, too. But there are not that many companies that know how to get their real story across.

Thomas Johnson, Vice President of Corporate Planning, Chemical Bank

Question: *Is a company's corporate image significant to you?*

Johnson: My prejudice is that image building without substance is of no value. We see around us each day companies trying to look good and spending money on appearance rather than substance. Before you develop a strategy for projecting the right kind of image, you must know (1) what you want to be; (2) relate that objective to your audiences, including first and foremost, the stockholder, then to the customer, whose welfare is tied to the stockholder, and finally to the public.

I have been more than peripherally interested in our program to finance upgrading apartment house incinerators and heating plants. That's a good example of our colleagues doing research a couple of years ago on pollution control and we're serious about wanting to have Chemical Bank make a genuine contribution.

Over the long run, these activities are essential. But you also need to understand how you may conflict, in the short run, with shareholders' interests. You need to know and measure the impact, to make an intelligent decision.

What we were trying to do in pollution control is to make a unique and genuine contribution, and our naive initial thought was philanthropic. But we found that making money available alone would neither do genuine good nor allow us to participate in helping with the approach. With research and the help of agencies, we found that (1) Local Law 14 is the Code governing incinerator and heating plant standards; and (2) lack of funds was being used as a surface excuse for lack of compliance. By putting the focus on this area of the problem in a public way and in addition making money available, we helped build the ground swell, so that money was no longer the issue, and thus we helped speed up compliance. Our thrust was to do something first, and, if there was something to talk about later, okay. We're tied to New York and so it may be easier for us to relate to our community than it is for some other companies.

Question: *In evaluating your corporate customers, to what extent are you influenced by their corporate image, reputation and posture?*

Johnson: From the point of view of investment of our funds, it's the substance of what funds will be used for that is more decisive than the market place impression of the company. For example, we don't make loans for purchase of arms by countries.

During a money crunch and high inflation, we had a strong policy against making loans for acquisitions. Thus, at the time of tight money, we seemed to be running our loan portfolio counter to the way the investing public was viewing companies; that is, conglomerates were just buying and changing leverage, and we tried to avoid participating in this inflationary process.

So far as our loan portfolio is concerned, we're not very much inclined to worry about the picture that companies present. We've been a bank that serves large corporations. The security of our loans would depend on their soundness—multi-product and multi-industry concerns. Thus a customer market shift would not have an enormous impact in the short run.

Question: *How and where do you pick up the emerging company? How do you plan for the development of corporate customers on a long run basis?*

Johnson: We've done a lot of thinking about this question, and we have found that without having searched fully in all ways, for us the most successful procedure has been to have the most intelligent and aware people representing our bank, and let them specialize in broad market segments (geographically), not in industries only. Of course, every bank covers a couple of industries in a specialized way, like petroleum.

Within our geographic orientation (and we have just rethought this carefully over a full year) and within the geographic groupings, we place emphasis on working closely with the communities outside New York through our diverse bank, corporate and commercial contacts.

There are many instances when this approach has paid off. For example, in high technology industries, we have found many companies whose money requirements had outgrown their local bank and so they came to us. What brings a company to the attention of our people and our specialists? That's harder to answer, because it's a variety of facts, and while formal communications may play a part, it would be hard to isolate.

Question: *What are your criteria for wanting a particular corporate customer?*

Johnson: In the long run, we want the company that has significant requirements for short-term and intermediate loans or financing and who wants access to overseas funds. For instance, the multinational company might want overseas long-term debt issues, which our bank can help underwrite.

Because of the banking industry price structure, we are not interested only in companies with short-term needs, who go to other long-term vehicles. We prefer customers who will have financing requirements we can fulfill in the long-run, although these customers may be in and out at varying times.

Because the nature of our lending portfolio is changing in favor of longer-term loans than seasonal, we look much more closely at (1) managerial strength; (2) marketing capabilities; and (3) project management. In strict seasonal financing, you can make a 90-day loan to support receivables, and you can look at short-term balance sheet information. Over the longer term, such as in building a plant, the balance sheet is much less relevant, because you must know the company's future ability to generate earnings and cash flows to both pay you back and come back as a customer.

We're always talking in terms of "paying us back," but we really mean "credit worthy" in the long run: (1) the ability to pay back and (2) developing an ability to support additional relationships and business with the bank.

We tend to favor customers whose needs go beyond credit needs. As a large money-center bank, we have a full line of services, and so we want those customers who can use these—pension trust appointments, lock box services, and so on.

Question: *As you watch corporate customers develop into major diversified giants, how do you feel about the suitability of their original name or any change in corporate name and identity?*

Johnson: A name change can be essential, and when it is part of an information strategy, it can be an excellent move. I think that the main legitimate reason for a drastic name change is to achieve some more representative identification of the present, and especially future status of your business. For example, a company that diversified out of a narrow industrial or geographic limitation may require such a change.

If there is a good reason like that, such as the old name being detrimental or limiting in the company's ability to attract business, then a change of name is essential. For instance, the Sioux Falls Grain company may have trouble getting British grain brokers to take it seriously.

But one of the things that irk me is companies who think up a grandiose name that tends to evoke a grandiose image completely out of line with the firm's activities. I am turned off by "Systems" and the high technology names that attempt to get the glamor to rub off to a higher P/E than they deserve. In the long run, only earnings count. Faith has a short life on Wall Street; maybe not as short as it ought to.

If you look at historic P/E's, you find a certain pattern. Every once in a while, the market P/E gets out of line and a company struggles to stay above the market P/E. The average obviously doesn't apply to each company, but there has to be some rational relationship.

Certainly corporate information, from name through all the communications activities, is very important. The point I'm making is only that these will work well when they're reflective of the company's capabilities and activities, not when they're an attempt to camouflage a lack of performance. I do think that a sound and sophisticated corporate communications program often reflects the thinking of an equally sophisticated management.

The Dollars and Cents Value of Corporate Image and Reputation

A company's "corporate image" has a measurable and significant effect on the price of its securities and the multiple that these securities command. Investor confidence in management is part and parcel of the corporate image, tightly linked to the company's over-all communications program, and recognized by Wall Street as an important influence. In fact, a strong corporate image can not only reinforce the positive impact of "good information" on its security price, but it can also mitigate the negative impact on its security price that might result from unfavorable news or information.

This conclusion represents more than an act of faith or the voice of experience. It is a contention that can be tested out statistically in the financial marketplace.

The company that has followed an intelligent and contemporary communications strategy aimed at the financial community will find that its security price and multiple can withstand the shock of "bad news" about the company far better and more resiliently than the company that has used ineffective communications in the past. In other words, an effective communications strategy, based on sound and current understanding of the investment community, acts as measurable insurance against a variety of preventable stock price fluctuations or declines in P/E multiples.

It is equally true that the company that executes consistently an intelligent communications program directed at the investing public will get more rapid and lasting mileage from the good news that its operations generate.

It is important, however, to distinguish between a sophisticated communications program and an avalanche of puffery. The latter is singularly suspect and ineffective among Wall Street sophisticates.

What then are the criteria of sophisticated corporate communications aimed at the investor today as contrasted with earlier years? And can these criteria be quantified?

There are a number of caveats to keep in mind in answering the first question:

1. Unlike earlier and simpler days, it is no longer possible to equate all visibility with good visibility. In the development of an effective communications strategy, it is essential to build a believable bridge between the company's past and its future.

Wall Street's memory, contrary to popular legend, is like that of the proverbial elephant. No corporate name change, for instance, no matter how drastic, will wipe out the memory of a dividend payment skipped, or management scandals assumed buried, or product failures considered historic. On the contrary, a blatant attempt to hide history is more likely to produce a dangerous credibility gap between investor and company management.

2. The old truism about every investor also being a consumer does little to guide a communications strategy. Both consumer and investor markets are highly segmented today, and the communications strategy that may produce the desired level of product sales and profits in the consumer marketplace can easily boomerang if applied directly to the investment community. The appropriate communications strategy for a company requires as sophisticated and specialized an understanding of the investment community as it requires knowledge and experience in the consumer marketplace.

3. It's not the quantity, but rather the quality of the communications effort that determines success. Every individual contact with the financial community—whether a conscious effort through letters, releases, mailings,

or unconscious through company signage, packaging, employee reputation—can either enhance the previously favorable reputation or undermine it.

The communications program and effort does require cohesion and harmony. But it would be naive to assume that such cohesion is accomplished through across-the-board corporate endorsement of every product or service sold by each corporate division, whether there is a sound marketing reason behind such endorsement or not. Rather, the cohesion of the communications program comes out of the logic of the underlying purpose, the soundness of the research upon which it is based, and the comprehension of company history and management plans for the future.

The same approach that worked yesterday may or may not work in today's dynamic financial and business community.

How can one quantify the impact of a sophisticated corporate communications program on Wall Street?

Theoretical models for testing these concepts are even now being developed in some of the leading graduate schools of business throughout the United States. But experience alone tells us what these models are designed to prove. For instance, in this year of divestitures and write-offs of disappointing corporate activities begun in the booming Sixties, we have all seen the divergent impact of this news on the securities of the varying companies involved. Such news received important attention in all the press. However, the effect on the various companies' stocks and multiples varied greatly.

The reason: The financial community today probes very carefully into the facts—not only those behind the financial figures, but also those behind the headlines.

How can a company make sure that it is communicating effectively with the investor community in today's context?

There are no simple guidelines that lend themselves to easy adaptation by any company. This contention becomes obvious when we consider the difference in the communications problems and objectives of the broadest categories of companies. For example, a consumer product manufacturer has a different type of opportunity for visibility than an industrial company. A consumer service company, such as an insurance company, airline or bank has a still different challenge from that facing the consumer product marketer.

Furthermore, it is generally difficult to keep even these broad lines drawn precisely in the light of post-World War II diversification.

However, even the company that has grown principally through product line extension, rather than diversification, might find it far more profitable to communicate its corporate strengths to the financial community differently than it stresses its product strengths to the consumer.

Perhaps the simplest way to distinguish between the appeal to the customer community and the appeal to the financial and investor community may be contained in the following truism:

The product or service customer is buying history. The investor is buying the future.

It is this distinction, well-thought out and thoroughly researched, that captures the essence of sophisticated communications strategies today.

The Grand Design for Magic Multiples

Years ago, *The New Yorker* ran a cartoon showing a tiny tot pushing away a spoonful of vegetable urged on him by a Helen Hockinson type of mother, who says, "It's broccoli, dear." The tot's answer, "I say it's spinach and the hell with it!"

The cartoon holds a moral for the company that tries to camouflage its pedestrian activities by puffery addressed to Wall Street. The investment community doesn't buy "glamor names" today. It buys management sophistication and the wisdom behind corporate plans for the future.

How can a company make sure that it is aiming the most appropriate and favorable communications at the complex and diversified investment community? Obviously, there is no single pat answer to this challenge.

The program that may be ideally suited to the industrial giant or specially tailored for the consumer service complex is likely to be completely wrong for a diversified consumer product company. Nor can the strategy of the successful consumer product giant be grafted on to its direct competitor without inestimable loss of effectiveness and credibility.

Management styles differ from one company to the next, transcending the possible similarity of products and markets. The corporate reputation and communications strategy should reflect this individuality. Communications skill is based on understanding the difference between one enterprise and its competitors, not only in the consumer marketplace, but also in the financial community.

From working in close partnership with leading corporations in every feasible product and service area, Lippincott & Margulies has distilled some guidelines for the corporation seeking to develop a more effective communications strategy aimed at investors:

1. A corporate communications strategy should take into account corporate history, present activities and plans for future growth. It cannot achieve a focus that the investment community will consider believable if it does not reflect understanding of both past and future. And as Gus Levy points out, "Credibility is essential."

2. A sound and up-to-date strategy has to be based on a close working relationship with corporate management and objective research in the field. Sophisticated opinion and market research will provide an important perspective for shaping strategy, and it will reveal the real areas of strengths that deserve essential policy back-up. Corporate action in these areas must either precede or coincide with communications. Gordon Williams expressed a pervasive Wall Street attitude when he said, "We are all turned off by a company that tries to make up in sheer volume for a lack of meaningful communications."

A clear statement of corporate growth objectives tends to be a springboard for research. However, Tom Johnson documents a Lippincott & Margulies' premise when he says, "before you develop a strategy for projecting the right kind of image, you must know (1) what you want to be; (2) relate that objective to your audiences, including the stockholder, then to the customer, whose welfare is tied to the stockholder, and finally to the public."

In this day of complex and conflicting attitudes, it may take multiphase research to relate corporate goals and hopes to the hidden motivations of the corporate customer, investment community, government audience, as well as the general public.

3. Research into present attitudes and needs is not enough for shaping corporate policy and corporate communications. It requires the tempering of knowledgeable insight. No amount of opinion and market research

alone can provide meaningful clues about future trends and thought patterns. Therefore, it is essential to anticipate which strains of current intellectual debate and which thoughts are likely to lead to actions that will affect tomorrow's business climate. An effective communications strategy must anticipate the future.

4. Cliches provide more comfort than insight; they lead to bad strategic choices. Thus, we know that bigness is considered bad today. Yet the effective and knowledgeable communicator knows how to turn bigness to advantage, how to uncover the buried corporate links to the local community, how to capitalize on local brand names without loss of ties to the far-distant corporate enterprise that owns the franchise.

5. "Conglomerization has outrun communication." Few companies have learned to create new types of communication geared to reflecting favorably the corporate motivation, planning and wisdom behind a seemingly jumbled complex of disparate products and services.

Historically, in American business, structure has followed strategy. Corporate conglomerization and diversification may still be too young for a real organizational pattern to emerge. Yet, the company that realizes its need to develop the appropriate valuation for its securities can't afford to wait for other companies to lead the way. It must create an effective communications strategy, if management is unwilling to let its P/E multiple be determined by the creative initiative of the Wall Street research community.

The consumer doesn't beat a path to the better mousetrap without considerable help through communications from the mousetrap manufacturer. By the same token, the investor won't beat a path to the undervalued stock without considerable help through communications from the management of the undervalued company. Being undervalued can also be an open invitation to the corporate raider or shrewder management team on the look-out for corporate bargains.

Only investor confidence and support, as exhibited by enthusiastic buying of a company's securities, will provide the financial muscle that makes it possible for management to carry out its plans for future growth. The challenge is gigantic in this decade when each company faces a diversified community of some 26 million different individual and institutional investors, and when each security competes with thousands of other listed and unlisted securities.

Management has the responsibility to face this challenge. And facing it well can bring tangible and measurable rewards.

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Conglomerates: Phase III

Why are some corporations burdened with the label conglomerate while others are looked upon as highly diversified? Why were conglomerates so badly hurt during the 1970-71 economic downturn? Discusses the severe communications gap confronting conglomerates today, and their future prospects.

Sense 64

American Motors

The dramatic turnaround of an ailing giant. How improved management techniques and a full-scale corporate communications program put American Motors back in the black and repositioned the company for more effective competition in the years ahead.

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The Vital Role of Communications in Mergers & Acquisitions

What's the most critical period in a merger or acquisition? Before? During? After? The often overlooked factor of corporate communications, its opportunities and problems. Detailed examination of each stage of corporate amalgamation, with useful checklists on what to do.

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